

Message Text

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12

ACTION NEA-16

INFO OCT-01 EUR-25 ISO-00 CIAE-00 DODE-00 PM-07 H-03

INR-11 L-03 NSAE-00 NSC-07 PA-04 RSC-01 PRS-01 SP-03

SS-20 USIA-15 AID-20 COME-00 EB-11 FRB-03 TRSE-00

XMB-07 OPIC-12 CIEP-03 LAB-06 SIL-01 OMB-01 FEA-02

INT-08 DRC-01 /192 W

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R 220611Z AUG 74

FM AMEMBASSY KUWAIT

TO SECSTATE WASHDC 0624

INFO AMEMBASSY ABU DHABI

AMEMBASSY BEIRUT

AMEONSUL DHAHRAN

AMEMBASSY DOHA

AMEMBASSY JIDDA

AMEMBASSY LONDON

AMEMBASSY MANAMA

AMEMBASSY MUSCAT

USMISSION OECD PARIS

AMEMBASSY TEHRAN

UNCLAS KUWAIT 3521

STATE PASS TREASURY

E.O. 11652: N/A

TAGS: EFIN, KU

SUBJECT: CREDIT SQUEEZE IN KUWAIT.

SUMMARY: A CREDIT SQUEEZE IS UNDERWAY IN KUWAIT THAT IS BEGIN-
NING TO AFFECT LOCAL ECONOMIC ACTIVITY. SQUEEZE RESULTS FROM
LEAKAGE OF KUWAITI DINARS WITH RESULT THAT DEMAND FOR DINARS
EXCEEDS SUPPLY. THIS IS RAISING COST OF CREDIT AND HAS HAD
RESULT OF CONSTRAINING BUSINESS ACTIVITY, NOTABLY SPECULATIVE
ACTIVITY IN SHARE MARKET. ALTHOUGH GOK PROBABLY WELCOMES SOME-
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WHAT DAMPENED LOCAL ECONOMIC ACTIVITY, WE ANTICIPATE THAT

BUSINESSMEN AND BANKERS WILL BEGIN TO PUT PRESSURE ON CENTRAL BANK TO DEVELOP INSTRUMENTS OR IN SOME OTHER MANNER RECYCLE KUWAITI DINARS BACK INTO LOCAL ECONOMY. END SUMMARY

1. LOCAL BANKERS TELL US THAT THERE IS A CREDIT SQUEEZE UNDERWAY IN KUWAIT THAT IS BEGINNING TO AFFECT LOCAL ECONOMIC ACTIVITY. ALTHOUGH GOK RECEIVING EXTREMELY LARGE PAYMENTS FROM OIL COMPANIES, LITTLE OF THESE FUNDS ARE ENTERING THE LOCAL MARKET. NORMALLY THE MOST SIGNIFICANT SOURCE OF NEW MONEY IS THE GOK EITHER THROUGH PURCHASE OF EQUIPMENT AND SERVICES, THROUGH WAGES, OR THROUGH ITS PROGRAM OF LAND PURCHASES. APPARENTLY, WHATEVER MONEY IS COMING INTO THE SYSTEM IT IS NOT SIGNIFICANT IN COMPARISON WITH KUWAIT DINARS THAT ARE FLOWING OUT OF THE SYSTEM. RESULT IS THAT THERE IS A SHORTAGE OF KD WHICH IS CURRENCY IN WHICH LOCAL BUSINESS IS TRANSACTED.

2. ACCORDING TO BANKERS, KUWAITI BUSINESSMEN AND INSTITUTIONS ARE CONVERTING THEIR KD TO DOLLARS AND OTHER FOREIGN CURRENCIES AND ARE PLACING DEPOSITS OUTSIDE KUWAIT TO TAKE ADVANTAGE OF HIGHER INTEREST RATES. IN KUWAIT, INTEREST ON LOANS IS HELD ARTIFICIALLY LOW (7 PERCENT), AND THEREFORE, LOCAL INTEREST RATES CANNOT RISE SUFFICIENTLY TO REFLECT ACTUAL DEMAND FOR CREDIT. APPARENTLY LOCAL BANKS HAVE MORE ASSETS THAN THEY DID A YEAR AGO, BUT A SMALLER PORTION OF THEIR ASSETS IS MADE UP OF KD. WE UNDERSTAND THAT IN THE LAST ELEVEN MONTHS TOTAL LOANS ARE UP KD 90 MILLION (KD 1 - \$3.38) WHEREAS NEW DEPOSITS ARE UP ONLY KD 30 MILLION. IN ADDITION, CENTRAL BANK OF KUWAIT INITIATED CERTAIN LIQUIDITY RESERVE REQUIREMENTS LAST SPRING.

3. NET RESULT OF THESE DEVELOPMENTS HAS BEEN TO DAMPEN, SOMEWHAT, DOMESTIC BUSINESS ACTIVITY. THROUGH FEES AND OTHER DEVICES, BANKS ARE CHARGING MORE FOR CREDIT DESPITE CEILING ON INTEREST RATES. LOCAL BANKS ARE MORE DISCRIMINATING IN PROVIDING LOANS TO BORROWERS. LOCAL SHARE MARKET WHICH WAS BECOMING HIGHLY SPECULATIVE EARLIER THIS YEAR HAS QUIETED CONSIDERABLY.

4. COMMENT: IT IS STILL A LITTLE TOO EARLY TO SAY WHAT THE OVERALL EFFECT OF THESE DEVELOPMENTS WILL BE. NEW WAGE INCREASES COULD MAKE A DIFFERENCE. EARLIER THIS YEAR, REGIONAL ECONOMIC OFFICER WAS TOLD BY BUSINESSMEN IN LOWER GULF THAT UNCLASSIFIED

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KUWAITI PRIVATE FUNDS WERE DRYING UP AND IT WAS THOUGHT THIS WOULD HAVE SOME IMPACT ON BUSINESS ACTIVITY THROUGHOUT THE GULF. IT APPEARS THAT SOME OF THE SPECULATIVE AND MARGINAL ACTIVITY OF SPRING HAS NOW ENDED AND LOCAL BUSINESSMEN WILL PROBABLY HAVE TO DELAY SOME OF THE PROJECTS THEY HAD BEEN THINKING ABOUT. WE THINK GOK ON BALANCE WILL WELCOME THESE MOVES SINCE OFFICIALS WERE BECOMING INCREASINGLY NERVOUS OF SPECULATIVE AND MARGINAL BUSINESS ACTIVITY. GOK WILL ALSO WELCOME EFFECT ON

INFLATION ALTHOUGH MAIN FORCE BEHIND INFLATION WILL REMAIN HIGHER PRICED IMPORTED GOODS.

5. THE BUSINESS COMMUNITY, HOWEVER, IS BEGINNING TO FEEL CONSTRICTED. BUSINESSMEN ARE BEGINNING TO COMPLAIN AND BANKERS ARE EXPRESSING NEED FOR NEW DEVICES TO HELP THEM IN THEIR PRESENT SITUATION. ONE YOUNG KUWAITI BANKER NOTED THAT KUWAIT CENTRAL BANK HAS NOTHING ANALAGOUS TO U.S. TREASURY BILLS. LOCAL BANKERS CAN, THEREFORE, BE EXPECTED TO BEGIN TO TRY TO GET THE CENTRAL BANK TO DEVELOP INSTRUMENTS OF THIS TYPE. THIS WOULD BE ONE MORE OCCASION IN WHICH THE BUSINESS COMMUNITY LOOKS TO CENTRAL BANK TO COME UP WITH SOLUTION FOR PROBLEMS ARISING OUT OF INCREASINGLY COMPLEX LOCAL ECONOMY. IN TURN, THE CENTRAL BANK WILL TAKE ON ADDED INFLUENCE AND POWER, ALMOST BY DEFAULT. IN THE ABSENCE OF ANY OTHER INSTITUTIONS WHICH IN A POSITION TO TAKE STEPS TO ALLEVIATE PROBLEMS FACED BY LOCAL BUSINESSMEN.
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